

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Robert G. Taub, Acting Chairman;
Tony Hammond, Vice Chairman;
Mark Acton;
Ruth Y. Goldway; and
Nanci E. Langley

Competitive Product Prices
International Business Reply Service Competitive
Contract 3 (MC2011-21)
Negotiated Service Agreement

Docket No. CP2013-78

ORDER APPROVING CONTINGENCY PRICING ARRANGEMENT

(Issued March 26, 2015)

I. INTRODUCTION

The Postal Service seeks to include a contingency pricing arrangement (Pricing Arrangement) pursuant to an International Business Reply Service Competitive Contract 3 (IBRS 3) agreement (Agreement) within the IBRS 3 product.¹ For the reasons discussed below, the Commission approves the Postal Service's request.

¹ Notice of United States Postal Service of Prices Under Functionally Equivalent International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, March 16, 2015 (Notice).

II. BACKGROUND

Agreements included within the IBRS 3 product permit U.S.-based businesses selling lightweight articles in foreign countries to offer their customers a convenient method of returning the articles to the United States for recycling, refurbishment, repair, or other value-added processing. The businesses supply postage-prepaid IBRS packaging to their foreign customers to return the used or defective articles. Pursuant to an IBRS Competitive Contract 3 agreement, the businesses pay the Postal Service a negotiated price for each returned article. An IBRS 3 agreement may also include a contingency clause allowing for modification of rates.²

On March 16, 2015, in accordance with 39 C.F.R. § 3015.5, the Postal Service filed its Notice, along with supporting documents. In the Notice, the Postal Service states that the Pricing Arrangement occurs under a surviving term of the Agreement, which expired September 30, 2014. Notice at 2. It further states that the Commission directed the Postal Service to file rate changes occurring as the result of such contingency with the Commission and to provide at least 15 days' advance notice of the change in rates. *Id.*

The Postal Service asserts that the Pricing Arrangement is functionally equivalent to the baseline agreement for the IBRS 3 product and requests that the Agreement be included within the existing IBRS 3 product. *Id.* at 2-3. Among the supporting documents, the Postal Service included a copy of the Governors' Decision authorizing the IBRS 3 product, a copy of a notice to the customer concerning the price adjustment, the Pricing Arrangement proposed to be added to the product, a certification of compliance with 39 U.S.C. § 3633(a), and financial workpapers. *Id.* at 3-4. In addition, the Postal Service submitted an application for non-public treatment of

² Docket No. CP2013-59, Order Approving New International Business Reply Service Competitive Contract 3 Agreement, April 15, 2013, at 5 (Order No. 1698).

materials requesting that unredacted portions of the Agreement, customer-identifying information, and related financial information remain under seal. *Id.* Attachment 4.

The Pricing Arrangement is intended to take effect April 1, 2015. Notice at 3. It is intended to remain in effect unless modified by the Postal Service. *Id.*

In Order No. 2400, the Commission provided public notice of the Postal Service's filing; established the instant docket for consideration of the filing's consistency with applicable statutory policies and Commission regulations; appointed a Public Representative; and provided an opportunity to comment.³

III. COMMENTS

The Public Representative filed comments on March 25, 2015.⁴ No other comments were received.

Based upon a review of the Postal Service's filing, including the information filed under seal with the Commission, the Public Representative concludes that the Agreement's contingency pricing remains functionally equivalent to the baseline agreement, despite "evident differences" between the original and contingency prices. PR Comments at 3. He also states that it appears the contingency prices shall generate sufficient revenues to cover costs and satisfy the requirements of 39 U.S.C. § 3633. *Id.*

IV. COMMISSION ANALYSIS

The Commission's responsibilities in this case are to ensure that the Pricing Arrangement: (1) is functionally equivalent to the baseline agreement established for the

³ Notice and Order Concerning International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, March 18, 2015 (Order No. 2400).

⁴ Public Representative Comments on Notice of United States Postal Service Prices Under Functionally Equivalent International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, March 25, 2015 (PR Comments).

IBRS 3 product; and (2) satisfies the requirements of 39 U.S.C. § 3633 and applicable Commission rules (39 C.F.R. §§ 3015.5 and 3015.7).

Contingent prices. Contingent pricing arrangements, like the one under consideration, typically provide the Postal Service with the flexibility to change rates without the need to enter into an entirely new agreement. In Order No. 684, the Commission determined that the Postal Service, when exercising this type of contingent pricing provision, must comply with Commission rules by filing the changed rates with the Commission in conformity with 39 C.F.R. § 3015.5.⁵ The Commission reiterated this condition in Order No. 1698. Order No. 1698 at 6. The Commission finds that the Postal Service's filing is consistent with both directives.

The Commission further finds that the Agreement, notwithstanding its expired status, specifically permits contingency price changes. The Commission also agrees with the Postal Service's observation that "the instant contingency prices are likely to apply to an extremely small number of postal items, due to the mailer's profile and the passage of time since the contract's expiration." Notice at 3.

Functional equivalence. In Order No. 684, the Commission added IBRS 3 to the competitive product list and designated an agreement as the baseline agreement for assessing the functional equivalence of agreements proposed for inclusion within the IBRS 3 product. Order No. 684 at 6. In Order No. 1698, the Commission found that the Agreement, which includes a contingent pricing clause, was functionally equivalent to the baseline agreement. Order No. 1698 at 5. A review of the Pricing Arrangement, which reflects the Postal Service's exercise of a contingency clause in the previously approved Agreement, leads to the conclusion that it is consistent with the Commission's finding of functional equivalence in Order No. 1698.

The Postal Service asserts that its filing demonstrates that the Pricing Arrangement is functionally equivalent to those contemplated in the IBRS 3 baseline agreement, and requests that the Agreement be included within the IBRS 3 product.

⁵ Docket Nos. MC2011-21 and CP2011-59, Order Approving International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, February 28, 2011, at 6 (Order No. 684).

Notice at 4-5. It asserts that the Pricing Arrangement is essentially identical to those envisioned in the IBRS 3 baseline contract in Docket Nos. MC2011-21 and CP2011-59, albeit with minor procedural variations due to different negotiation outcomes. *Id.* at 4. It asserts that the nature of the IBRS service provided in the letter that is the subject of this docket and in the IBRS baseline agreement is essentially the same, and the instant IBRS Pricing Arrangement bears similar market characteristics to other IBRS Competitive Contract 3 agreements. *Id.* The Postal Service also incorporates by reference its arguments regarding functional equivalence in Docket No. CP2013-78.⁶

The Commission has reviewed the Postal Service's reasons for asserting that the Pricing Arrangement is functionally equivalent to the baseline agreement and comports with 39 U.S.C. § 3633 and applicable Commission rules. It also has considered the Public Representative's comments. The Commission concludes that the Pricing Arrangement is substantially similar to the baseline agreement and that the differences between them do not fundamentally alter either the service the Postal Service will provide under the Agreement or the structure of the Agreement. The Commission therefore finds that the Pricing Arrangement may be included within the IBRS 3 product.

Cost considerations. The Commission reviews each competitive product to ensure that it covers its attributable costs, does not cause market dominant products to subsidize competitive products as a whole, and contributes to the Postal Service's institutional costs. 39 U.S.C. § 3633(a); 39 C.F.R. §§ 3015.5 and 3015.7. As long as the revenue generated by a product exceeds its attributable costs, the product is unlikely to reduce the contribution of competitive products as a whole or to adversely affect the ability of competitive products as a whole to contribute an appropriate share of

⁶ See Notice of the United States Postal Service Filing of a Functionally Equivalent International Business Reply Service Competitive Contract 3 Negotiated Service Agreement, August 29, 2013, at 4-6. Some of the differences the Postal Service identified between the baseline Agreement and the Agreement include a revision concerning the duration of the Agreement; the addition of a phrase concerning the possible filing of contract revenue, cost, or volume data in other Commission dockets; and the addition of an article concerning intellectual property, co-branding, and licensing. *Id.* at 5-6.

institutional costs. In other words, a product that covers its attributable costs is likely to comply with 39 U.S.C. § 3633(a).

The Commission has reviewed the Postal Service's filing, including supporting financial analyses provided under seal, and the Public Representative's comments. Based on this review, the Commission finds that the Pricing Arrangement should cover its attributable costs. The addition of the Pricing Arrangement to the IBRS 3 product will not cause cost coverage for the product to fall below 100 percent because, as the Commission found in the FY 2013 Annual Compliance Determination (ACD), the product as a whole covers its attributable costs.⁷ Consequently, the Commission finds that the addition of the Pricing Arrangement to the IBRS 3 product should allow the product to continue to comply with 39 U.S.C. § 3633(a)(2). Because it finds that the addition of the Pricing Arrangement to the IBRS 3 product should allow the product to cover its attributable costs, the Commission finds that the addition of the Pricing Arrangement to the product should not result in competitive products as a whole being subsidized by market dominant products, in accordance with 39 U.S.C. § 3633(a)(1). Similarly, it finds the addition of the Pricing Arrangement to the IBRS 3 product is unlikely to prevent competitive products as a whole from contributing an appropriate share of institutional costs, consistent with 39 U.S.C. § 3633(a)(3). Accordingly, a preliminary review of the Pricing Arrangement indicates it is consistent with section 3633(a). The Commission will review the Pricing Arrangement's cost coverage, the cost coverage of the IBRS 3 product, and the contribution of competitive products as a whole to the Postal Service's institutional costs in the ACD to ensure that they continue to comply with 39 U.S.C. § 3633(a).

Rate changes. The Agreement, like previous IBRS competitive agreements, includes clauses addressing cost increases and contingent pricing that allow the Postal Service flexibility to change rates without entering into a new agreement. The Commission addressed the implications of contingency pricing clauses in Order No. 178

⁷ Docket No. ACR2013, Annual Compliance Determination Report, March 27, 2014, at 86-91.

and concluded that the Postal Service must file notice of rate changes occurring under such clauses pursuant to 39 C.F.R. § 3015.5 and provide a minimum of 15 days' notice.⁸

Other considerations. The Pricing Arrangement is to remain in effect unless the Postal Service chooses to modify the rates. Notice at 3. Any future rate modification pursuant to the contingency clause in the Agreement is to be filed in conformity with 39 C.F.R. § 3015.5.

The Postal Service shall promptly notify the Commission of the effective date of the Pricing Arrangement. Upon termination of the Pricing Arrangement by either party, the Postal Service shall promptly file notice of such termination with the Commission in this docket. In addition, within 30 days of the termination of the Pricing Arrangement, the Postal Service shall file costs, volumes, and revenues associated with the Pricing Arrangement in this docket.

V. ORDERING PARAGRAPHS

It is ordered:

1. The Pricing Arrangement filed in Docket No. CP2013-78 is included within the International Business Reply Service Competitive Contract 3 (MC2011-21) product. The revision to the Mail Classification Schedule appears below the signature of this Order and is effective immediately.
2. The Postal Service shall promptly notify the Commission of the effective date of the Pricing Arrangement.
3. The Postal Service shall promptly file notice in this docket of the Pricing Arrangement's termination.

⁸ Docket Nos. MC2009-14 and CP2009-20, Order Concerning International Business Reply Service Contract 1 Negotiated Service Agreement, February 5, 2009, at 10 (Order No. 178).

4. Within 30 days of the termination of the Pricing Arrangement, the Postal Service shall file costs, volumes, and revenues in this docket.

By the Commission.

Shoshana M. Grove
Secretary

CHANGES TO THE MAIL CLASSIFICATION SCHEDULE

The following material represents a change to the Mail Classification Schedule. The Commission uses two main conventions when making changes to the Mail Classification Schedule. New text is underlined. Deleted text is struck through.

Part B—Competitive Products

2500 **Negotiated Service Agreements**

2515 **Inbound International**

2515.3 **International Business Reply Service (IBRS) Competitive Contracts**

2515.3.5 **Products Included in Group (Agreements)**

Each product is followed by a list of agreements included within that product.

- International Business Reply Service Competitive Contract 3

Baseline Reference

Docket Nos. MC2011-21, CP2011-59

PRC Order No. 684

Included Agreements

CP2013-78 (contingency pricing arrangement), expires ~~March 31,~~
~~2015~~TBD
